

CRAFTING STRATEGY To IMPROVE XYZ RICE MILLING BUSINESS COMPETITIVENESS

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Abstract— East Java rice milling business has been affected by a series of political policy regarding the industry, and increasing raw material purchase competition. This article is concerned about current competitive condition facing XYZ; it is experiencing problem of declining profitability even though the market is in uptrend. This decline is represented by problems in material purchase, production efficiency, and low selling price. The study and is aimed towards improving XYZ competitiveness and profitability. The literature review provided some generic framework in analyzing business condition and developing strategy (Wheelen & Hunger, 2012). Research is conducted by interviewing, observation of XYZ owner, and through secondary data gathering. Result of the research is analyzed to determine elements of business environment affecting XYZ. External analysis of the company point out strategic factors potentially important to the company such as market requirement of premium rice, differing price between east and west java, as well as notable price discrepancy between area in East Java. Internal analysis of XYZ point out important strategic factors that affect XYZ in terms of its competitiveness, such as the relatively outdated production method and low direct sales effort of XYZ. From SWOT analysis of these factors, it is concluded that problem affecting XYZ competitiveness is requirement for reformulating business strategy. Based on it, a strategy is formulated for XYZ to improve competitiveness by upgrading production machinery, improve material purchase, and increase direct sales. It is concluded that the main problem of XYZ is low efficiency, and it is recommended that XYZ implement the solution to improve its competitive readiness and to prepare for future challenge.

Keywords: business strategy, rice milling business, business model, TOWS matrix

1. Introduction

XYZ is a rice milling business currently operating in Sidoarjo, East Java. XYZ has been experiencing increase in competitive condition. XYZ experience increasing competition in material purchase indicated by utilization rate of 90%, low production efficiency with expected inefficiency of Rp 55 per kg, and lower selling price of the product with the difference reaching up to 10 per cent of selling price. XYZ needs a strategy, to overcome these problems.

A. Company History

XYZ is a family business, established by the founder, father of the current owner, in the 80's in Sidoarjo, East Java. In around 2010, control of the business shift to one of the founders son, while ownership transferred equally to the sons of the founder. Currently, XYZ employs 18 employees and is operating in green.

B. The Rice milling business

Traditionally, rice milling activities was conducted separately from rice trading activities. Some rice milling businesses mainly process unhulled rice into hulled rice, and deriving its main revenue from processing fee received. However, some development in technology causes some rice milling business owner to adopt different business model, that instead of relying on the processing fee only, it also involved itself in rice trading activities.

Rice business also affected by the fact that rice is a strategic resource for Indonesian, since rice is currently the main staple food of Indonesian. Strategic importance of rice was indicated by a survey

(Kementrian Pertanian RI, 2012) which placed rice first in terms of annual per capita consumption at about 90 kgs. This strategic position makes it a prime interest of Indonesia government, which subjects it to several regulation and implementation. Although rice business itself is not tightly regulated, some government policy directly affects it, such as the rice import policy and establishment of bulog buying price.

C. XYZ Scope of Business

XYZ operation revolves around rice milling business and rice trade. It conduct operation surrounding the rice milling process such as unhulled rice purchasing, rice milling process, and sales of end product (rice) and its by product (bran, husk). To sell its main production output, XYZ maintain partnership with rice agent customer from rungkut area, Surabaya. Some of its main production output is sold through store attached to the milling plant. The byproduct is sold through collector that comes to the plant. In its operation, XYZ also maintain partnership with other rice mills in the area, especially when it comes to material procurement which sometimes was distributed unevenly due to differing harvest season between rice producing area.

D. Business Issue of XYZ

XYZ is experiencing decline in profitability. Some indicator to the problems are increasing competition when purchasing material, and competition when selling end product. Competitors especially from western area continue to purchase material at higher price due to the higher end product selling price at western java. This condition affects XYZ in that it is currently operating at 90 per cent capacity. Although the figure is still high, if left not addressed, the problem could grow worse since the trend of material purchase is expected to increase. Price difference between east and west java reached up to Rp 1000. The condition is also further affected by current east java governor to place rice import restriction in east java. On the other hand, selling price between the producer level and consumer level could differ up to 10 per cent. Selling to agent level has been primary means of XYZ to distribute its production output, and the margin for selling to agent is notable thin.

Aside from the input and output aspect of the production, some issues also comes from the production process itself. A persisting assumption about efficiency of the current traditional process has inhibited any effort to upgrade the current production machinery albeit XYZ's ability to finance the upgrade. This has proven to limit production capacity at certain time through bottlenecking in the production, especially during harvest period, causing some loss of potential profit. Potential cost of inefficiency in production process is estimated at Rp 55 per kgs. The combined business issue at the input, process, and output point of the production currently is still in manageable level. However, those issues have potential to severely affect XYZ business in the future, and XYZ needs a strategy to address these issues before it develops even further.

2. Business Issue Exploration

In this part, author attempts to explore elements and factors contributing to the business issue faced by XYZ. Exploration of the business issues will be structured according to the framework laid out initially. It is expected that the factors contributing to rise of the business issues could be identified, and the root cause could be determined.

E. Conceptual Framework

To assist with identifying factors contributing to business issues, and determining the root cause of the problem, a framework will be used. The framework will follow concept laid out by Wheelen and Hunger (2012) regarding business strategy formulation, and business model concept by Osterwalder (2010). The framework separated the study into three stages: Environmental scanning stage, strategy formulation stage, and implementation stage. Environmental scanning stage attempts to analyze factors that affects and having potential to affect XYZ in the future. Factors analyzed come from external, industrial, and internal

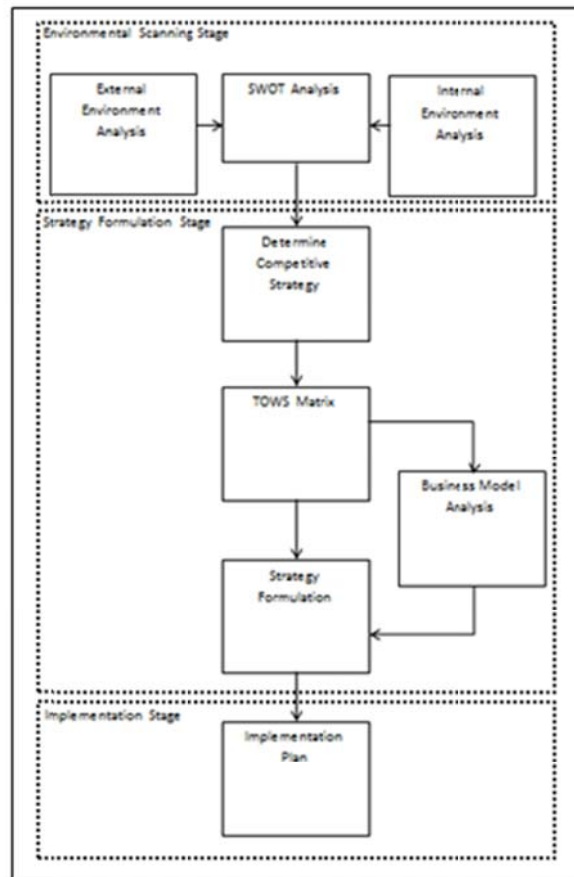


Figure 1 Conceptual Framework of the Study

XYZ. External scanning analyzes PEST (Political, economic, socio-cultural, and technological) factors for trend affecting rice milling business. Porter's five forces framework is then used to analyze competitive situation in the industry. Internal analysis of XYZ is conducted by reviewing resource and competencies of XYZ, and through analysis of rice business value chain to identify factors that contribute to strengths and weaknesses of XYZ.

From scanning of external and environmental factors, a SWOT analysis will be conducted to assess XYZ's business opportunities, threats, strengths, and weaknesses, and to determine root cause of issues facing XYZ. Based on the analysis conducted in the environmental scanning stage, a competitive strategy is developed as the basis of the strategic direction of XYZ. A set of alternative strategies will be generated by using TOWS matrix tools. Business model is then strengthened, and the strategy formulated. At the implementation stage, the implementation plan for the proposed strategy is developed.

F. Method of Data Collection and Analysis

To analyze factors according to the framework, primary data for the study is collected through interview and observation of XYZ owner. Secondary data is obtained through literature review of past studies. Results of the interview and literary studies are then used to conduct analysis according to framework of the study.

G. Analysis of Business Situation

As mentioned in the framework section, environmental scanning analyze business situation at three points: external, industry competitive situation, and internal. External analysis is conducted through PEST factors analysis. And as part of the external analysis, industry analysis also conducted using

Porter's five forces framework for industry analysis (Porter, 1980). The analysis provided several notable external factors, which then summarized into External Factors Analysis Summary (EFAS). Most notable factors are:

- Technological development provided both opportunities and threat. An opportunity present for efficiency of up to Rp 55 per kg processed.
- Price discrepancy between areas in east java presents opportunities, if the barrier could be breached. The difference is as high as Rp700-1000
- Development of premium market presents opportunities for selling higher quality rice at increased price. 40 per cent east Javanese is expected to be in this category.
- Price gap caused by market structure difference between eastern and western area causing some western player to purchase in east java. Spread reach up to Rp 1000.
- Five forces analysis suggested that current rice business industry competitiveness is: medium

Internal scanning as part of the scanning, conducted by analyzing resource and competency of XYZ, which the followed by value chain analysis of XYZ activities (Crain and Abraham, 2008). Some notable factors identified during the analysis included as follows:

- Good presence and relationship with nearby farmer provides partial material supply security, which contribute to XYZ strengths. Over 20 years presence.
- Relationship with agent customer with potential to absorb 200 per cent of current production output of XYZ.
- Low direct sales, contribute only up to 30 per cent total sales
- Inefficient production method, cost about Rp 55 per kgs material processed.

Results gathered from external and internal scanning are summarized into EFAS and IFAS respectively, and through SWOT analysis, root cause of the problem is identified.

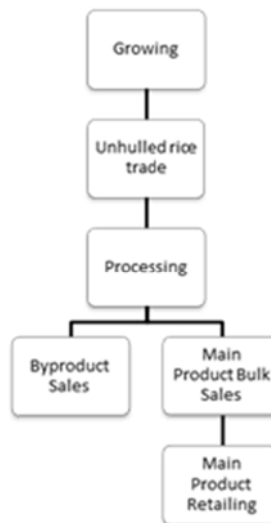


Figure 1. Rice Business Simplified Value Chain

Table 1. Relative Vs Potential Value Adding of XYZ

Value Adding Activities	Value Adding Potential	Value Adding realized through current activities
Growing	Medium	No activities
Unhulled Rice Trade	Low - Medium	Low

Processing	Low	Minimal
Byproduct Sales	Medium	Medium
Main Product Bulk Sales	Low	Low
Main Product Retailing	High	Low

Problems facing XYZ are:

1. Deteriorating competitiveness against western buyer in material purchasing due to differing price level between east and west java
2. Traditional production method is relatively inefficient and relatively low capacity compared to the more modern method.
3. Lower selling price, with up to 10 per cent difference with retail price.

The first cause is external factor which is difficult to control, while the second and the third cause is internal factors that XYZ might be able to address internally. Root cause of problem facing XYZ could be inferred as "low efficiency of XYZ activities."

3. Business Solution

To determine the business solution, several alternatives has been developed, and to be analyzed in determining one optimal solution for XYZs business issue. The solution would not be analyzed one by one, but the focus would be on a particular strategy proposed for implementation.

H. Alternative of Business Solution

In line with the framework, first, a strategic positioning needs to be determined to align strategies of XYZ that are to be proposed, to provide theme for those strategies. Analysis of the appropriate strategy is conducted by reviewing the SWOT analysis conducted in the previous stage. Elements included in the SWOT analysis are assigned into the most appropriate strategy that support that factors according to its weight. Some factors supporting specific strategic positioning are:

- Customer perceived price as among the most important effect: cost-leadership
- Lower sales price at distributor level: cost-leadership
- Inefficient current production method: cost-leadership

Overall analysis showed support for implementation of cost leadership strategy. Other supporting factors for implementation of cost leadership strategy are:

- Rice is highly commoditized, and there isn't much room for differentiation of product. In this case, cost leadership is the best choice.
- Price discrepancy between areas open up possibility for the rice milling business to market its product to the area with higher price level for additional profit.
- The differing market condition with western part causes price difference, and a strong cost leadership would be required to compete effectively when purchasing material.

Along with determination of strategic positioning, a strategic concept is developed as part of the competitive strategy. The concept is: "improve efficiency of activities", which fits well into cost leadership positioning of business activities to improve competitiveness.

To generate strategies alternatives, a TOWS matrix is used. Some strategies generated by the TOWS matrix is presented in figure 3. In strategy formulation, some of the strategies developed will be proposed for implementation.

I. Analysis of Business Solution

Among the identified strategy alternatives, there are several alternatives considered as the most potential one to be applied. This is due to the alternatives being in line with strategic concept proposed before.

		Internal Factor Analysis Summary (IFAS)	
		Strengths	Weaknesses
CV.XYZ Rice Milling		<ul style="list-style-type: none"> • Relative presence and network in the area • Strong Indirect selling network • APG engagement • Capital reserve • Material purchasing team 	<ul style="list-style-type: none"> • Direct selling ability • Sales network • Production method • Product development capability • Regional orientation
External Factor Analysis Summary (EFAS)	Opportunities	SO Strategies	W-O Strategies
	<ul style="list-style-type: none"> • Price discrepancy among area, barrier • Requirement for premium rice • Modern milling method available • Modern drying technique 	<ul style="list-style-type: none"> • Develop product to enter premium-packaged market • Invest to upgrade production process • Invest to improve drying technique • Aim purchase to area with historically good crop quality 	<ul style="list-style-type: none"> • Increase direct sales to end customer. • Establish store to increase market penetration in high price level area • Improve production quality
	Threats	S-T Strategies	W-T Strategies
	<ul style="list-style-type: none"> • Raw material availability • Threat of new entrant • Food diversification program • Differing price between east and west • Inflation 	<ul style="list-style-type: none"> • Establish formal network management procedure with farmers • Strengthen purchasing team capability to cover more area of operation • Strengthen indirect marketing channel 	<ul style="list-style-type: none"> • Improve production and selling efficiency.

Figure 2. TOWS Matrix for Strategy Alternatives Generation

Along with the strategy alternatives generation, strengthening of business model is conducted by addressing XYZs elements of business model to support strategic positioning of XYZ. Strengthening through innovation in business model building blocks are as follows:

- The innovation is offer driven, in which new value proposition of: Fluffiness, aroma, physical feature, and price
- The offer will require change in activities and resources required by XYZ, which include procurement of higher quality material and improvement in production process capability to produce quality output.
- Customer segment will be focused towards serving end customer, although the agent level customer is still served.
- Revenue will increase due to profit from direct selling; cost is expected to be controlled through efficiency incorporated into changes in activities conducted.

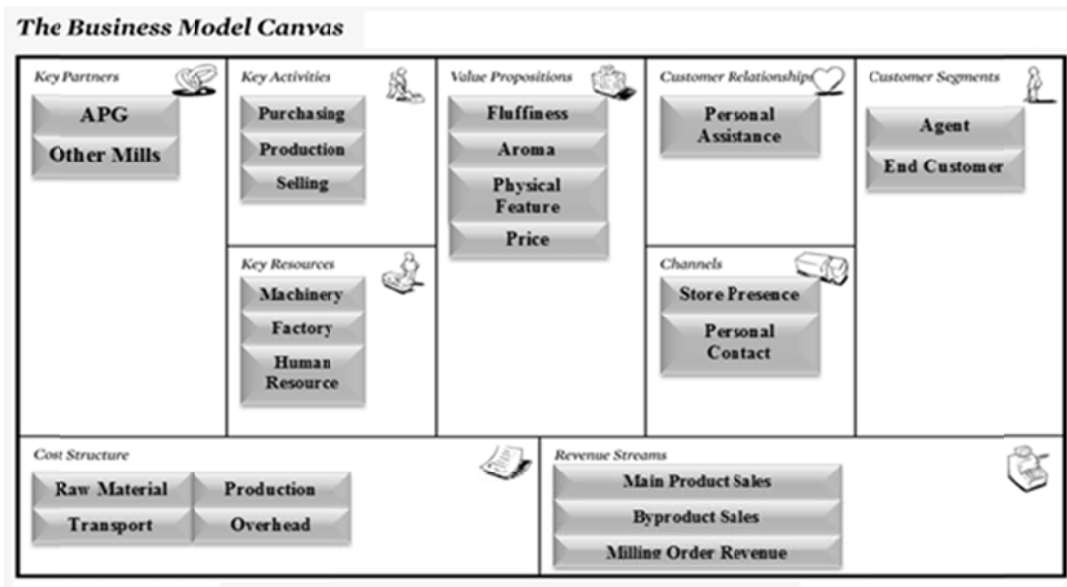


Figure 4 Proposed Business Model of XYZ

The next step according to the framework is business formulation. In the business formulation, strategies alternative generated through TOWS matrix is selected for strategies that is coherent with business model proposed. Some strategies generated through TOWS matrix are not selected due to the conflicting element with the strategic concept. Another reason for not selecting strategies included:

- Development of new product to enter premium market: XYZ is poor if not incapable of new product development. Implementation of this strategy is difficult.

Three selected prominent strategy from strategies generated by TOWS matrix are: opening new store to support direct sales, strengthening of purchasing team through increase in team size and quality control for material purchased, and increase production efficiency through modernization of production machinery. Some reasons supporting selection of these strategies are:

- XYZ already have some experience in direct selling, and some network albeit small, in the targeted area (Malang). Whether the new store opened in Malang or Sidoarjo depends on the XYZ ability to penetrate barrier between Malang and Sidoarjo.
- Modernization of equipment will provide benefits of increase in installed production capacity, reduced overhead cost, reduced preprocessing cost, and increase in quality of produce (such as reduced percentage of broken).
- Currently, XYZ employs 9 buyer and increased buyer would be required if XYZ is to modernize its equipment which is expected to increase installed production capacity. Along with increase in production, quality of material purchased could be increased also.
- Current consumer network is prepared to absorb double the current capacity. It is safe to increase production capacity and material purchased

However, selected strategies have some managerial implications that might affect XYZ. These managerial implications should be kept checked if the strategies are to be implemented successfully. Those implications are:

- Upgrading production machinery entails some risks and downtime during the upgrade project, which may affect XYZ severely.
- With the current sales structure, competing with western area during material purchasing is difficult. Some new purchaser also might needs some time to adjust, so reliability of the material supply will be fluctuating for some time. Establishment of quality control for material purchased also may took some time before implemented effectively.

- Opening of new store entails higher degree of risk than simply expanding production capacity. A careful planning should be exercised, and it should be done as the final option after upgrade and purchaser expansion is done.

4. Conclusion and Implementation Plan

The strategies entails three action plans: opening of new store, upgrade of production machinery, and strengthening of purchasing team and activities. Responsibility for successful implementation of the strategy will be taken by the owner; however, each of the corresponding function will provide support during the action plan execution.

- Production will support the machinery upgrade action plan, which scheduled from Q3 2013 to Q3 2013
- Store team will help the opening of new store, scheduled to be carried out from Q1 2014 to Q1 2015
- Purchasing team will help in strengthening the purchasing team strategy, scheduled to goes hand in hand with machinery upgrade between Q3 2013 and Q2 2014.

As a summary of the study, analysis of the business condition pointed out the problem of declining profitability, and a strategy was formulated to overcome the problem. It can be concluded that:

- Some external and internal factors are identified to directly affect XYZs competitiveness.
- To effectively mitigate external effect, and improve internal condition, new business strategy was formulated along with innovation in how XYZ conduct its business.

It is recommended for XYZ to implement the strategy to overcome current problem and prepare XYZ for future challenge in rice milling business.

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